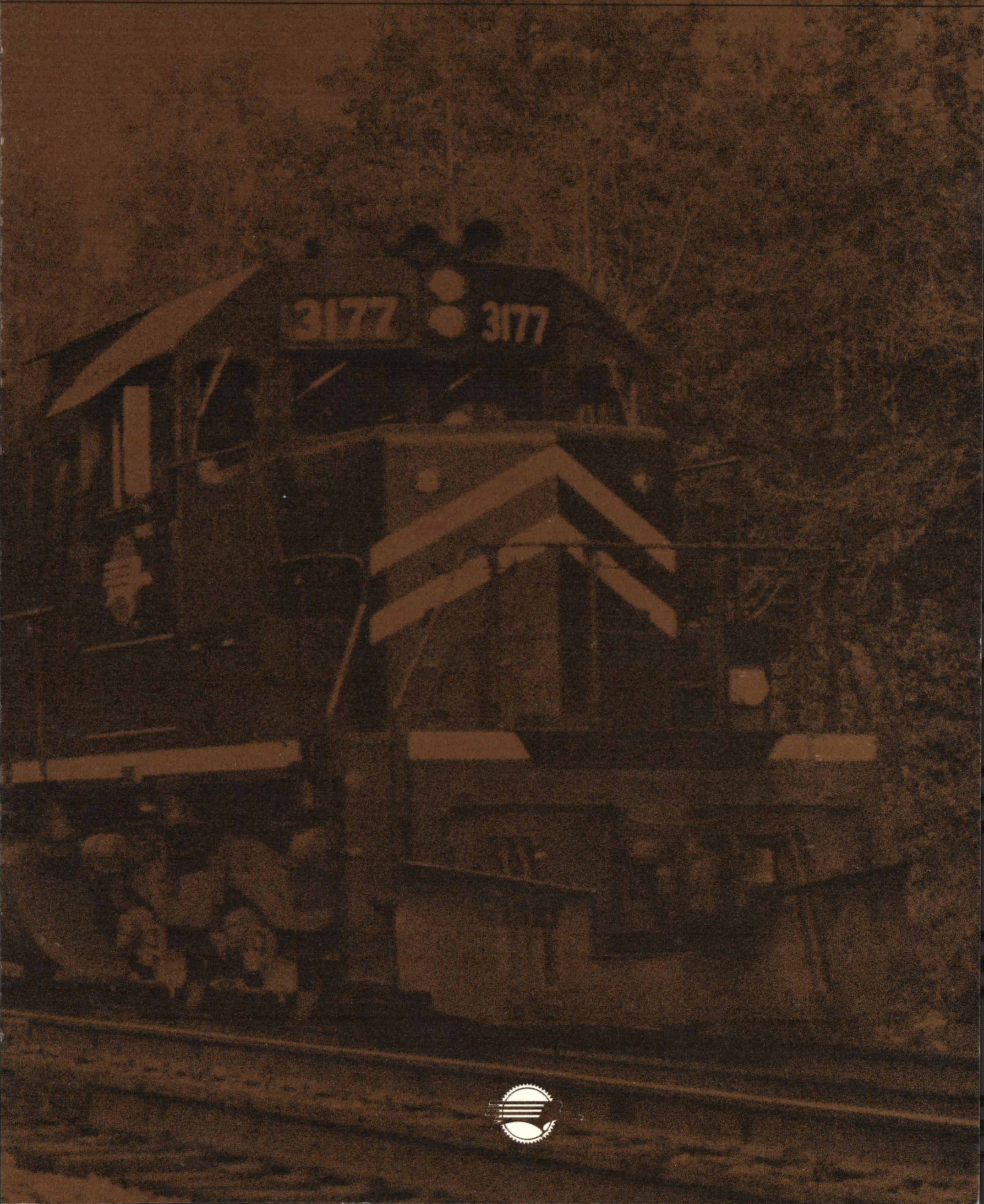
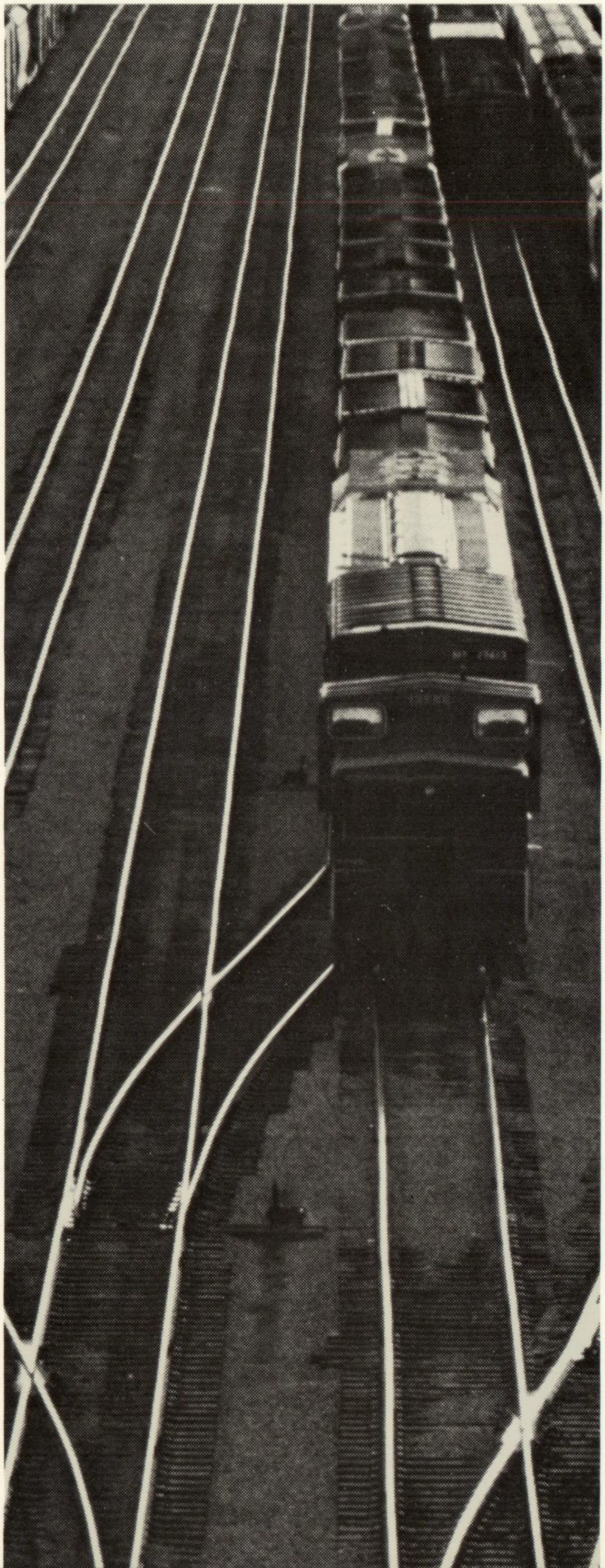
MISSOURI PACIFIC RAILROAD SYSTEM

1976

ANNUAL REPORT



MISSOURI PACIFIC SYSTEM



TRANSFER AGENTS

$1 Cumulative Convertible
Preferred Stock and
Common Stock

**UNITED STATES
TRUST COMPANY
OF NEW YORK**
45 Wall Street
New York, N. Y. 10005

**THE BOATMEN'S
NATIONAL BANK
OF ST. LOUIS**
100 N. Broadway
St. Louis, Mo. 63102

REGISTRARS

$1 Cumulative Convertible
Preferred Stock
and Common Stock

**MANUFACTURERS
HANOVER TRUST
COMPANY**
4 New York Plaza
New York, N. Y. 10004

**ST. LOUIS UNION
TRUST COMPANY**
510 Locust Street
St. Louis, Mo. 63101

DIVIDEND DISBURSING AGENT

$1 Cumulative Convertible
Preferred Stock and
Common Stock

**THE BOATMEN'S
NATIONAL BANK
OF ST. LOUIS**

**ANNUAL MEETING
OF STOCKHOLDERS**
The Second Tuesday in May
General Offices
Missouri Pacific Building
St. Louis, Mo. 63103

BOARD OF DIRECTORS

CLEVELAND PUBLIC LIBRARY
BUSINESS INF. BUR.
CORPORATION FILE

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President, King Ranch, Inc., ranching, Kingsville, Texas

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President, The Central Trust Bank, Jefferson City, Mo.

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Senior partner of the law firm of Smith, Williams, Friday, Eldredge & Clark, Little Rock

****HERBERT GUSSMAN**
Independent oil producer and investments, Tulsa

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Vice President and General Counsel, Missouri Pacific Railroad, Executive Vice President, Missouri Pacific Corp., St. Louis

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ROMULO O'FARRILL, JR.
Chairman of the Board, Televisa S.A. (television station operation), Vice President and Editor-in-Chief of seven Mexican newspapers, Vice President, Impresora Y Editora Mexicana (magazine publishing and printing), Vice President, Automotriz O'Farrill (automobile distribution), Mexico City

*††**THOMAS H. O'LEARY**
President, Missouri Pacific Corp., which controls subsidiaries involved in railroad operations (Missouri Pacific System), production/transmission of natural gas and cement manufacturing, St. Louis

***W. M. SHAPLEIGH**
President, Ralston Purina Co., diversified food processor, St. Louis

***HAROLD E. THAYER**
Chairman of the Board and Chief Executive Officer, Mallinckrodt, Inc., manufacturers of chemicals and pharmaceuticals, St. Louis

▪**F. B. WADELTON**
President, The Insco Systems Corp., data processing services, Neptune, N.J.

*Executive Committee
†Finance Committee
▪Audit Committee
**Chairman of Executive Committee
††Chairman of Finance Committee

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Chairman of the Board, St. Louis

J. H. LLOYD
President and Chief Executive Officer, St. Louis

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Executive Vice President, St. Louis

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Vice President and General Counsel, St. Louis

W. R. McDOWELL
Vice President and General Counsel (Southern Lines), Dallas

J. A. AUSTIN
Vice President-Traffic, St. Louis

R. K. DAVIDSON
Vice President-Operation, St. Louis

J. G. GERMAN
Vice President-Engineering, St. Louis

J. M. TOLER
Vice President-Transportation, St. Louis

D. L. MANION
Vice President-Administration, St. Louis

T. D. RODMAN
Vice President and Controller, St. Louis

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Vice President, Washington, D.C.

C. J. MAURER
Secretary and Treasurer, St. Louis

Consolidated Financial and Operating Highlights

for the year ended December 31, 1976

	1976	1975
Income and Expense Items:		
Operating Revenues	$1,013,668,000	$888,546,000
Operating Expenses	747,242,000	667,694,000
Operating Ratio (Rail Line)	72.3%	73.5%
Income Available for Fixed Charges	147,482,000	113,263,000
Times Fixed Interest Earned	4.1	3.3
Net Income	68,696,000	46,715,000
Earnings Per Common and Common Equivalent Share	5.40	3.74
See Page 17 for Information Relating to the Calculation of Earnings Per Share		
Financial Position:		
Gross Capital Expenditures	$ 131,041,000	$103,959,000
Depreciation and Retirements Charged to Income	45,964,000	45,334,000
Working Capital	45,282,000	24,190,000
Long Term Debt	753,025,000	740,746,000
Stockholders' Equity	532,717,000	465,842,000
Freight Statistics:		
Miles of Railroad Operated	11,674	11,718
Revenue Ton Miles (1,000's)	45,755,953	42,864,865
Revenue Per Ton Mile (cents)	2.06	1.93
Employees:		
Total Amount of Payroll	$ 372,596,000	$335,117,000
Average Annual Wages	17,664	15,781
Average Number of Employees	21,094	21,235

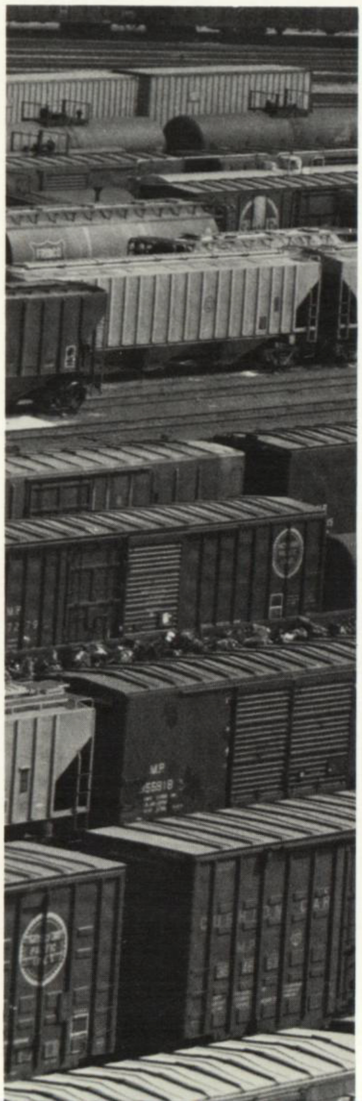
FINANCIAL/ CORPORATE

RECORD REVENUES AND EARNINGS

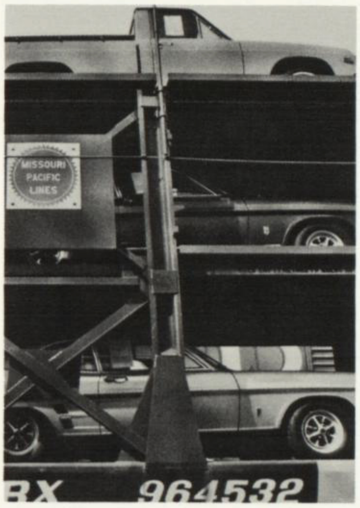
The Missouri Pacific System recorded the highest net income in its 125-year history during 1976 and surpassed $1-billion in revenues for the first time. Moreover, Mo-Pac invested a record $131-million in capital improvements, while lowering its operating ratio — the relation of expenses to revenues — from 73.5 in 1975 to 72.3 in 1976.

Missouri Pacific System consolidated net income for 1976 totaled $68,696,000, or $5.40 per share, compared to $46,715,000, or $3.74 per share, a gain of 47 per cent over 1975, which had been the second best year financially in Mo-Pac history.

Consolidated operating revenues advanced from $888,546,000 in 1975 to $1,013,668,000 in 1976.



Freight rate increases averaging 5.3 per cent became effective at various dates between March and October. However, the additional revenues accruing from the rate increases were virtually offset by increased prices for materials, supplies and wages. Another increase of 4 per cent was granted to the industry in January, 1977. The latest increase will help meet higher wages and fringe benefits which became effective at the first of the year.



Dividends paid per share of Common Stock totaled $1.25 in 1976 compared to $1.20 the previous year while dividends paid per share of Preferred Stock amounted to $1.

During 1976, the rating of Missouri Pacific Railroad equipment debt securities was raised to AA by Standard and Poor's and, during the prior year, to Aa by Moody's.

MERGER ACTIVITY

Merger of The Texas and Pacific Railway and the Chicago & Eastern Illinois Railroad into the Missouri Pacific Railroad was consummated on October 15, following approval by the Interstate Commerce Commission. Since the three properties had been operating as an integrated system, there were no significant changes as a result of the merger. Stockholders of the three railroads approved the merger overwhelmingly in 1974. Involved in the transactions were approximately 973,000 shares of Mo-Pac Common.

Missouri Pacific Corporation, parent company of Mo-Pac Railroad, and the Southern Railway Company mutually initiated studies in April to determine the feasibility of common corporate ownership and control. In a joint statement on September 15, the two companies announced termination of the discussions, saying that while benefits could be realized in a number of areas, they were unable to agree on financial terms.

STOCK EXCHANGE AND CONVERSION

On January 17, 1977, the Company completed redemption of all Preferred shares outstanding at the rate of $20 per share plus any dividends due. The stockholder, however, also had the right to convert each share of Preferred for one share of Missouri Pacific Railroad Common Stock.

SALES/ MARKETING/ SERVICE

MO-PAC TOPS INDUSTRY TREND

In addition to registering a gain of 13.8 per cent in gross freight revenues, Mo-Pac also attracted substantial new on-line industry, strengthened its marketing organization and added new trains to serve customers more efficiently.

For the year 1976, revenue ton-miles advanced 6.8 per cent on Mo-Pac compared to an estimated increase of 5.3 per cent for the railroad industry. Mo-Pac also retained its share of the rail freight market in the Central/Western districts of the U.S.A. at better than 17 per cent. Revenues rose in 11 of Mo-Pac's top 12 commodity areas.

CHEMICALS, AUTOS AND COAL WERE STRONG

Chemicals, which comprise about 20 per cent of Mo-Pac revenue, registered an increase of 19.2 per cent in revenues during 1976. Grain revenues rose slightly despite lower levels of traffic stemming from a fall in export grain contracts and a retention of unusually high amounts of grain in farm and elevator storage.

Automobiles and auto parts revenue, third most important market to Mo-Pac, rose 35.6 per cent. A revenue gain of 19.8 per cent was recorded in food products traffic and a revenue increase of 10.7 per cent occurred in the category of piggyback, freight forwarder and shipper association traffic. Fabricated metals traffic revenues declined 11 per cent while revenues for metal ores rose 10.6 per cent.

In other important markets, lumber revenues rose 31.3 per cent; paper was up 14.8 per cent; petroleum products increased 17.9 per cent and non-metallic minerals revenue advanced 16.3 per cent.

Coal, one of Mo-Pac's most rapidly expanding markets and seventh largest revenue source, showed an increase of 32.2 per cent in revenues. Even though on-line coal traffic was down because of miner strikes and mechanical problems at mines and handling facilities, the overall trend was up in 1976 as a result of increased long-haul traffic from the West.

INDUSTRIAL GROWTH CONTINUES

New industry, an important source of additional revenues, continued to locate along Mo-Pac tracks in key growth areas. During 1976, industry spent an estimated $1.1-billion in capital investment for 169 new or expanded facilities. Based on present rates, these firms could produce as much as $41-million in annual traffic revenues.

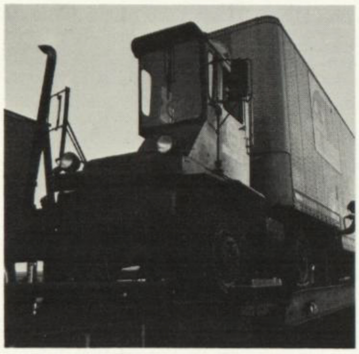
MARKETING REORGANIZED

A new Marketing Research Department, with expanded functions, was created in February, 1976, to replace the former Traffic Research Division. The purpose is to improve marketing strategies in competing for traffic with other transport modes as well as other railroads. Involved in the reorganization was assigning of specialists in specific commodity categories with augmentation of staff with personnel from sales, operations and data systems. Pricing personnel attracted substantial volume of new chemical, woodpulp, rice, sugar and auto parts traffic through creation of attractive rate packages.

NEW TRAINS ADDED

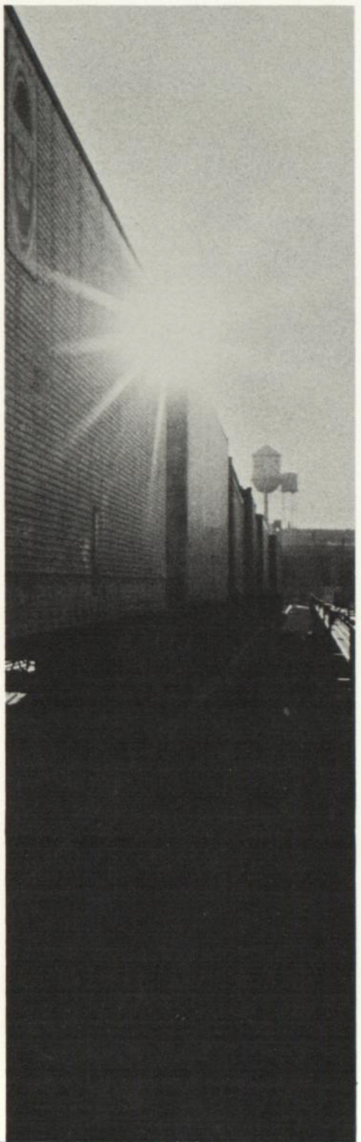
Three new unit train operations were added during the year to handle western coal moving from Utah, Colorado and Wyoming to points in Illinois and Oklahoma. A fourth new coal unit train was established between Southern Illinois and Chicago. All four are run in conjuction with connecting railroads.

INTERMODAL OPERATIONS



COMEBACK IN PIGGYBACK

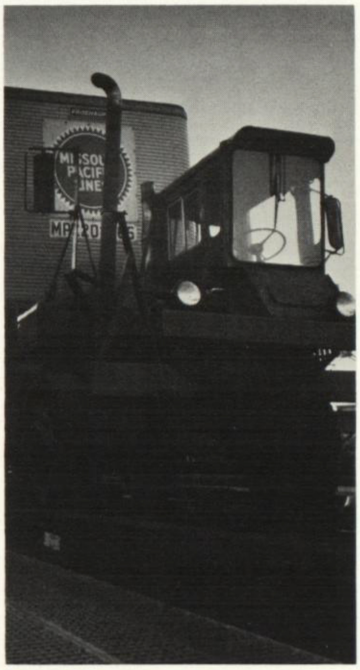
Both piggyback and container traffic grew in 1976 after declining in 1975, a trend common to the entire railroad industry. Piggyback trailer loadings increased 13.9 per cent in 1976, slightly above the industry average, while container shipments were up nearly 22 per cent. Actually, the piggyback growth trend was somewhat better than the railroad average because nationally railroads were coming back from a 19 per cent decline in 1975 while Mo-Pac was down only 12 per cent. In 1977, a substantial portion of Mo-Pac's advertising and direct marketing effort will be devoted to expansion of piggyback with emphasis on private truck fleet owners and high-volume on-line cities.



TRUCKLINES REVENUE IMPROVES

Total revenues for Missouri Pacific's two wholly-owned trucking subsidiaries were $41,748,000 in 1976, compared to $34,824,000 in 1975. This included revenue of $27,493,000 from sources other than services performed for the parent railroad. The gains are attributed to reorganization of the trucklines sales force and increased emphasis on import/export traffic and interline traffic with connecting motor carriers. The past year was the first full year that Mo-Pac trucklines operated as a full motor common carrier. Prior to an Interstate Commerce Commission order granted in 1975, Mo-Pac trucklines were confined to substitute rail service.

Application to merge The Texas & Pacific Motor Transport Company into Missouri Pacific Truck Lines was filed with the ICC on December 2, 1976. A favorable decision may be forthcoming during the first half of this year. The merger is a continuation of the corporation simplification program involving merger of the railroad operations of Mo-Pac.



MISSOURI PACIFIC AIRFREIGHT EXPANDING

Missouri Pacific Airfreight expanded its forwarding operations. New stations were opened at New York, San Francisco and Los Angeles, raising to 14 the number of inbound-outbound airfreight stations. Expansion to at least four more major cities is anticipated in 1977.

MODERNIZATION

RECORD CAPITAL EXPENDITURES

Capital expenditures for new freight equipment and numerous physical improvement projects reached a record level of $131,041,000 in 1976. Planned investment in capital improvements will exceed that amount in 1977. Company management is convinced that a continuing modernization program geared at handling increased traffic is a key to profitability and has been guided by this philosophy during the past 15 years.

New equipment investment totaled $97,747,000 in 1976. Equipment acquired during the year included 2,507 new freight cars and 65 locomotives. More than half of Missouri Pacific's freight car fleet has been purchased since 1961 while nearly 75 per cent of the locomotive fleet has been acquired since that year.

TRACK AND PHYSICAL STRUCTURES UPGRADED

During 1976, Mo-Pac laid 494 miles of new and relay rail, most of it continuous welded rail, and will lay about the same amount in 1977 with emphasis on Western District lines where track is being upgraded to handle new coal traffic moving in heavy unit trains. In addition, Mo-Pac installed 1,545,000 crossties; applied 1,826,000 cubic yards of ballast and resurfaced 7,700 track miles. Fifteen new bridges were constructed totaling 2,378 lineal feet. Production of ballast at the Gads Hill, Mo. plant was more than doubled to 1,000,000 tons. More than 24 miles of track was converted to Centralized Traffic Control in Illinois.

NUMBER MESSAGE LINES UNTIL DELETION REQUESTED
NUMBER MESSAGE LINES ALL THE
MOVE STATUS DISPLAY FORWARD ONE FRAME
HOLD DYNAMIC DISPLAY - DO NOT UPDATE
UPDATE DYNAMIC DISPLAY
DISPLAY PROGRAM FUNCTION KEY LINE
ERASE MESSAGE LINES SPECIFIED IN OPTION
ERASE MESSAGE LINE NN OR NN THROUGH NN
ERASE FLAGGED MESSAGES
ERASE OUT-OF-LINE STATUS DISPLAY
ERASE MESSAGE LINE NUMBERS
ERASE PROGRAM FUNCTION KEY LINE
DISPLAY ALL SPECIFICATION VALUES
ENTER
CANCEL

Among building projects completed during the year were a new office building at Villa Grove, Ill., a new yardmaster's tower at St. Louis and a new yardmaster's tower at St. Joseph, Mo. Underway was construction of a new intermodal terminal, office and yardmaster's tower at Shreveport, La. Intermodal facilities at Chicago are being expanded to accommodate increased traffic. Automobile facilities at Arlington, Texas, also were expanded.

Projects scheduled for 1977 include a new consolidated freight car repair shop at Dupo, Ill. near St. Louis and new yard offices at Natchez, Miss., Mineola and Dallas, Texas. Automobile facilities will be expanded at Chicago and Port Allen in the Baton Rouge, La., area. Intermodal facilities will be expanded at Memphis.

COMPUTER SYSTEMS EXPANDED

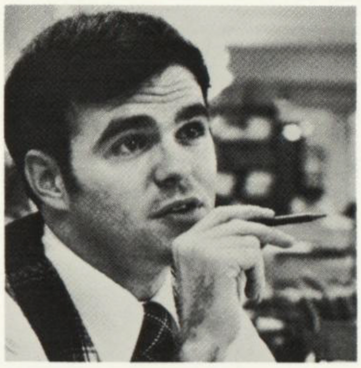
Mo-Pac became the first major railroad in the nation to have a totally centralized waybill rating system with completion of installation of AutoBill. This system not only permits highly automated computer preparation of shipping waybills and bills of lading but increases the efficiency of calculating freight charges through centralizing this function at St. Louis instead of having rate clerks located throughout the railroad system.

Mo-Pac's Transportation Control System was improved and expanded and further refinements were made in the Operations Control Center where a substantial part of the data from TCS is utilized in the planning and operation of transportation services. YATS, an electronic perpetual inventory system used to keep track of cars in yards, was expanded to five more locations as well as to the Alton & Southern Railway, a terminal switching line in East St. Louis which is 50 per cent owned by Mo-Pac. Six more Customer Service Centers also were installed. These centers enable shippers to carry out most of their business with Mo-Pac by telephone with the service center in their area.

PEOPLE

KEY MANAGEMENT CHANGES

Three men were elected to the board of directors, replacing outgoing members. They are: J. H. Clement, King Ranch president, Kingsville, Texas; H. H. Friday, attorney, Little Rock, Ark. and Romulo O'Farrill, Jr., publisher and businessman, Mexico City.

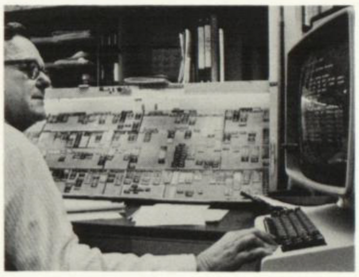


James W. Gessner was elected executive vice president. Richard K. Davidson, former assistant vice president-Operation, succeeded Gessner as vice president-Operation. Judy C. Durand was elected vice president at Washington, becoming the first woman to hold a vice presidency on a major U. S. railroad. She was formerly executive representative at Washington.

RECRUITING AND EMPLOYEE EDUCATION

Recruiting of able young college graduates continued in 1976 with 37 persons joining the management development program. In keeping with Mo-Pac policy of positive implementation of equal opportunity employment, both women and members of ethnic minority groups were included among those joining not only the management development program but other areas of railroad employment. In addition, women began working in such non-traditional jobs as switchperson, mechanical apprentice and locomotive engineer trainee.

Approximately 300 persons attended schools at all levels under the Company's tuition aid program whereby half the cost of tuition is underwritten by Mo-Pac. Another 21 persons completed special orientation programs conducted by Mo-Pac, including a significant number of transportation people from Japan and Mexico. In addition, Mo-Pac continued to conduct special seminars for the training of sales personnel and for supervisors in the Operating Department.



THE FUTURE

The future, both the coming year and the years ahead, continues to look bright for Mo-Pac. We expect to finish 1977 with still another record for revenue and net income, barring economic catastrophe.

Industrial expansion within our territory will continue at a brisk pace, especially within the chemical industry.

Coal traffic should show substantial growth in 1977, particularly western coal. Mo-Pac is expanding facilities to handle rapidly growing automobile and auto parts business. We also anticipate that a substantial quantity of grain held in storage during 1976 will move to market in 1977.

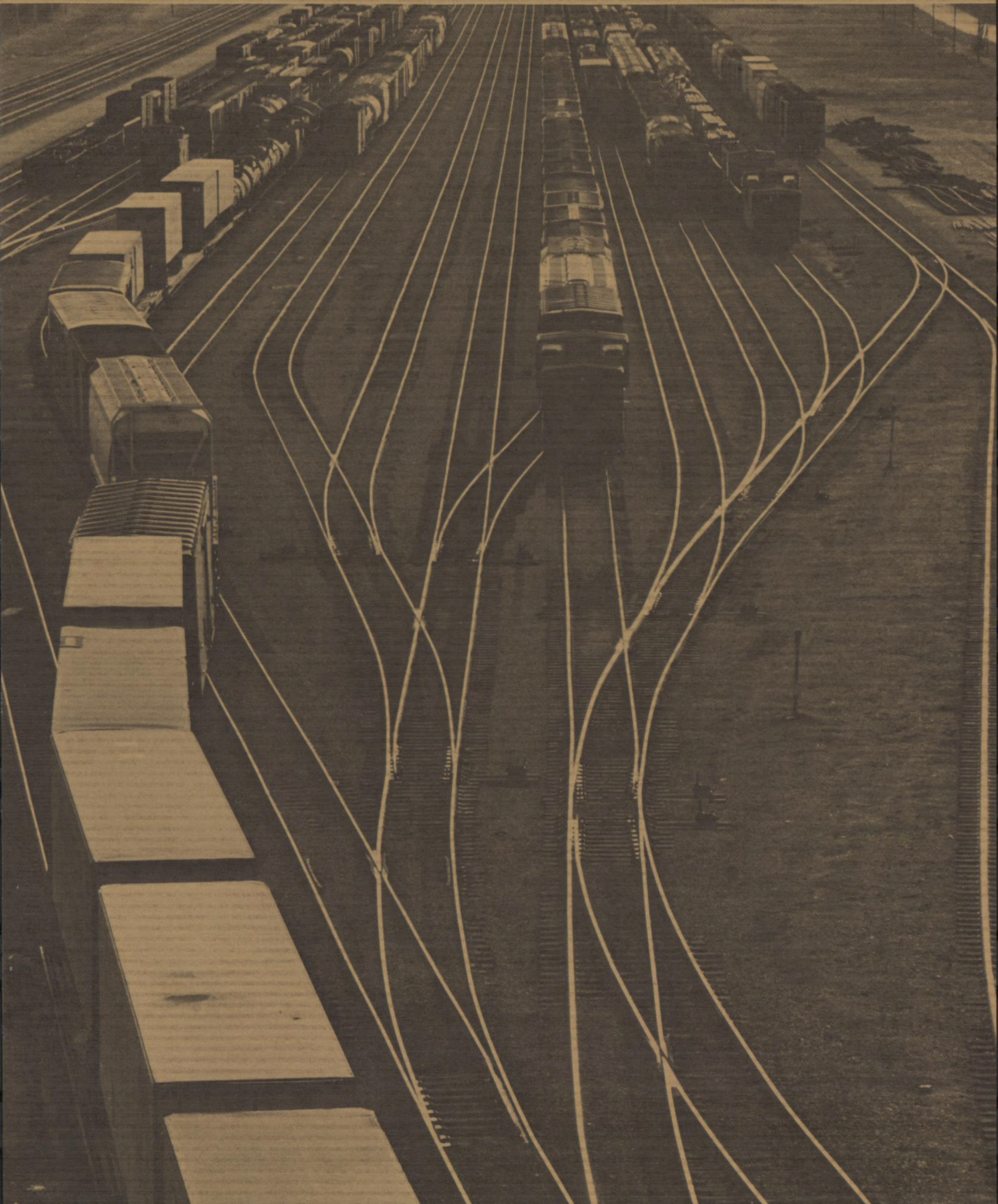
The railroad property is in excellent condition and its fleet of freight cars and locomotives is among the best in the industry. Our carefully-planned capital expenditures program during the past 15 years has proven to be a good investment by enabling the railroad to provide fast, reliable service and improve its competitive position. We also are experiencing numerous benefits through implementation of the Mo-Pac Transporation Control System and through our Operations Control Center.

JH Lloyd

John H. Lloyd
President and Chief
Executive Officer

February 25, 1977

MISSOURI
PACIFIC
SYSTEM



ANNUAL REPORT FORM 12-K TO SECURITIES AND EXCHANGE COMMISSION

Interested stockholders may obtain a copy of the Missouri Pacific Railroad annual report, Form 12-K, and a description of its exhibits filed with the Securities and Exchange Commission for the year ended December 31, 1976. A copy of this report may be obtained upon request after April 30, 1977, at no charge by writing to:

Office of Vice President and Controller
Missouri Pacific Railroad Co.
210 N. 13th Street
St. Louis, Mo. 63103

A copy of the exhibits can be obtained by marking a checklist, which will be enclosed with our reply, and prepayment of a reasonable fee.

QUARTERLY FINANCIAL INFORMATION — UNAUDITED*

(In Thousands of Dollars Except Per Share Data)

			First	Second	Third	Fourth	Total
Operating Revenues	1976...		$246,173	$253,897	$253,841	$259,757	$1,013,668
	1975...		216,965	210,882	215,597	245,102	888,546
Net Operating Income	1976...		25,608	29,795	30,837	39,025	125,265
	1975...		19,351	22,671	24,883	36,709	103,614
Net Income	1976...		14,626	15,295	15,122	23,653	68,696
	1975...		6,532	7,484	11,027	21,672	46,715
Earnings Per Common and Common Equivalent Share	1976...		1.17	1.22	1.21	1.80	5.40
	1975...		.52	.60	.88	1.74	3.74
Dividends Paid Per Share							
Common	1976...		.30	.30	.32½	.32½	1.25
	1975...		.30	.30	.30	.30	1.20
Preferred	1976...		.25	.25	.25	.25	1.00
	1975...		.25	.25	.25	.25	1.00
Stock Exchange Prices							
Common Stock							
American Stock Exchange	1976	High	30½	32½	32	32	
		Low	17¾	27⅝	27⅝	27⅜	
	1975	High	15	17½	16⅝	18½	
		Low	11	13¾	13¼	14	
Preferred Stock							
New York Stock Exchange	1976	High	30	32⅛	31½	32¼	
		Low	17¾	27½	27½	27	
	1975	High	14¾	17½	16¼	18¼	
		Low	10¾	13⅝	13¼	13¼	

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*The 1975 interim financial information was not subjected to a limited review by the Company's independent accountants.

Statement of Consolidated Income

(In Thousands of Dollars)

	Year Ended December 31,	
	1976	1975
Operating Revenues:		
Freight	$ 981,005	$858,676
Switching and Other	32,663	29,870
Total Operating Revenues	1,013,668	888,546
Operating Expenses: (Notes 1 and 5)		
Maintenance of Way and Structures	140,098	121,211
Maintenance of Equipment	159,338	137,531
Traffic	19,669	18,123
Transportation	390,355	357,324
General	37,782	33,505
Total Operating Expenses	747,242	667,694
Net Revenue from Operations	266,426	220,852
Other Operating Charges: (Note 6)		
Taxes (Except Federal Income Taxes)	79,661	66,147
Equipment and Joint Facility Rents	61,500	51,091
Total Other Operating Charges	141,161	117,238
Net Operating Income (Before Federal Income Taxes)	125,265	103,614
Other Income (Net):		
Gain on Reacquisition of Long Term Debt	6,726	535
Other, Net	15,491	9,114
Total Other Income	22,217	9,649
Income Available for Fixed Charges (Before Federal Income Taxes)	147,482	113,263
Interest:		
Fixed	35,991	34,115
Contingent	9,782	9,986
Total Interest	45,773	44,101
Income Before Federal Income Taxes and Minority Interests	101,709	69,162
Provision for Federal Income Taxes: (Note 3)		
Current	17,863	14,340
Deferred	12,183	5,492
Total Federal Income Taxes	30,046	19,832
Income Before Minority Interests	71,663	49,330
Less — Income Applicable to Minority Interests	2,967	2,615
Net Income	$ 68,696	$ 46,715
Earnings Per Common and Common Equivalent Share (Notes 1 and 2)	$ 5.40	$ 3.74
Depreciation and Retirement Charges Included Above (Note 1)	$ 45,964	$ 45,334

See Notes to Consolidated Financial Statements, Pages 16-21

CONSOLIDATED BALANCE SHEET

Assets

(In Thousands of Dollars)

	Dec. 31, 1976	Dec. 31, 1975
Current Assets:		
Cash and Temporary Cash Investments	$ 116,833	$ 88,314
Deposits for Interest, Dividends and Equipment Acquisition	14,403	5,511
Accounts Receivable	76,264	76,876
Material and Supplies, at average cost	47,675	39,687
Accumulated Deferred Federal Income Tax Benefits	18,036	14,818
Other Current Assets	2,164	2,328
	275,375	227,534
Properties: (Notes 1 and 2)		
Road	890,276	935,171
Equipment	1,040,661	972,050
Miscellaneous	39,022	35,829
	1,969,959	1,943,050
Less:		
Accumulated Depreciation		
Road	135,813	134,278
Equipment	387,655	372,573
Miscellaneous	12,364	11,807
Excess of Net Assets (at acquisition) of Consolidated Subsidiaries Over Carrying Value of Investments		53,819
	1,434,127	1,370,573
Other Assets and Deferred Charges:		
Investment in Terminal and Other Companies (Note 1)	41,923	41,713
Capital, Insurance and Other Funds (Note 7)	20,697	27,547
Other	6,843	4,692
	69,463	73,952
	$1,778,965	$1,672,059

Liabilities

(In Thousands of Dollars)

	Dec. 31, 1976	Dec. 31, 1975
Current Liabilities:		
Accounts and Wages Payable	$ 108,494	$ 106,156
Current Maturities of Long Term Debt	39,642	35,398
Unmatured Interest Accrued	16,434	15,877
Interest and Dividends Payable	6,824	8,138
Federal Income Taxes Accrued	7,377	8,073
Other Taxes Accrued	19,826	13,656
Other Current Liabilities	31,496	16,046
	230,093	203,344
Long Term Debt (Page 14)	753,025	740,746
Other Liabilities and Deferred Credits:		
Accumulated Deferred Federal Income Taxes	203,232	187,830
Casualty Reserves and Other Liabilities (Note 7)	59,898	51,842
	263,130	239,672
Equity of Minority Stockholders in Consolidated Subsidiaries (Note 2)		22,455
Stockholders' Equity: (Note 4)		
$1 Cumulative Convertible Preferred Stock — No Par Value; Authorized 10,000,000 shares; Outstanding 156,560 and 5,717,903 shares, respectively	3,131	114,358
Common Stock — No Par Value; Authorized 15,000,000 shares; Outstanding 13,323,202 and 6,789,087 shares, respectively	201,031	76,185
Capital Surplus	1,451	1,451
Retained Income (Page 14)	327,104	273,848
	532,717	465,842
Commitments and Contingent Liabilities (Notes 6 and 7)		
	$1,778,965	$1,672,059

See Notes to Consolidated Financial Statements, Pages 16-21

Statement of Consolidated Retained Income

(In Thousands of Dollars)

	Year Ended December 31, 1976	1975
Balance at Beginning of Year	$273,848	$240,894
Add — Net Income	68,696	46,715
	342,544	287,609
Deduct — Cash Dividends —		
Preferred Stock — $1.00 Per Share	2,471	6,238
Common Stock — $1.25 Per Share in 1976 and $1.20 Per Share in 1975	12,969	7,523
Balance at End of Year (Note 4)	$327,104	$273,848

See Notes to Consolidated Financial Statements, Pages 16-21

Long Term Debt (Including Maturities in 1977)

(In Thousands of Dollars)

	Interest Rate	Date of Maturity	Changes 1976 Issued	Changes 1976 Reduction	Outstanding December 31, 1976 (excluding amounts held by Company)
Missouri Pacific Railroad Company					
First Mortgage Bonds (1)	4¼%	1990 & 2005		$15,325	$229,057
First Mortgage Bonds	5%	2000			18,961
First Mortgage Bonds (1)	3⅝%	1980		2	1,427
Second Mortgage Bonds	5%	2000			4
General Mortgage Bonds (1)	4¾% (2)	2020 & 2030		1,346	101,808
General & Refunding Mortgage Bonds (1)	3⅞%	1985		2,455	4,208
Income Debentures	5% (2)	2045			100,016
Income Debentures (1)	5%	2054			1,704
Equipment Obligations	4% to 11¼%	1977 to 1991	$73,843	30,391	312,625
Bank Loan		1976		6,000	
Majority-Owned Subsidiaries	4½% to 9%	1977 to 1995	3,543	5,344	22,857
Grand Total			$77,386	$60,863	$792,667

	1977	1978	1979	1980	1981
Long Term Debt Maturing During Each of the Next Five Years	$39,642	$36,988	$35,746	$35,220	$31,940

(1) Have annual sinking fund requirements. (2) Contingent interest.
Substantially all properties are covered by liens of the mortgages or under the equipment obligations.

Statement of Changes in Consolidated Financial Position

(In Thousands of Dollars)

	Year Ended December 31, 1976	Year Ended December 31, 1975
Financial Resources Were Provided By:		
Net Income	$ 68,696	$ 46,715
Add — Charges (Credits) Against Income Not Requiring Working Capital —		
Depreciation and Retirements	45,964	45,334
Increase in Long Term Casualty and Other Reserves	8,755	6,892
Deferred Federal Income Taxes	15,401	6,619
Income Applicable to Minority Interests	2,967	2,615
Gain on Reacquisition of Long Term Debt	(6,726)	(535)
Other, Net	15	1,450
Working Capital Provided from Operations	135,072	109,090
Salvage from Property Sold or Retired	8,195	7,199
Proceeds from Equipment Obligations Issued	73,843	55,927
Proceeds from Other Long Term Debt Issued	3,543	
Capital Fund Deposit Decrease	7,205	
Insurance Deposit Decrease		855
Other, Net		821
	227,858	173,892
Financial Resources Were Used For:		
Property Additions	131,041	103,959
Reduction of Long Term Equipment Obligations	39,158	35,792
Repayment of Long Term Debt	13,075	744
Reduction of Long Term Bank Loan	6,000	3,000
Dividends (Including Amounts Paid Minority Interests)	15,677	14,443
Capital Fund Deposit Increase		10,519
Other, Net	1,815	
	206,766	168,457
Increase in Working Capital	$ 21,092	$ 5,435
Analysis of Changes in Working Capital:		
Cash and Temporary Cash Investments	$ 28,519	$ 5,488
Accounts Receivable	(612)	4,681
Material and Supplies	7,988	3,701
Accumulated Deferred Federal Income Tax Benefits	3,218	1,127
Other Current Assets	8,728	(119)
Accounts and Wages Payable	(2,338)	(2,537)
Current Maturities of Long Term Debt	(4,244)	(2,945)
Federal Income Taxes Accrued	696	(1,627)
Other Current Liabilities	(20,863)	(2,334)
Increase in Working Capital	$ 21,092	$ 5,435

See Notes to Consolidated Financial Statements, Pages 16-21

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Principles of consolidation — The accompanying consolidated financial statements of the Missouri Pacific System include the accounts of the Missouri Pacific Railroad Company and its majority-owned subsidiaries. Investments in less than majority-owned terminal railroad companies (joint ventures) and other affiliated companies, where the Company has the ability to exercise significant influence over their operating and financial policies, are accounted for under the equity method.

Revenue recognition — Freight revenues are recognized upon completion of service.

Properties — Properties are stated primarily at estimated original cost, as determined by January 1, 1955 Interstate Commerce Commission valuations, plus additions and betterments at cost and less retirements since the dates of valuations.

The companies follow the straight-line method of depreciation using various group rates prescribed by the Interstate Commerce Commission. Depreciation provisions during 1976 and 1975 were at rates of approximately 3.8% and 3.7%, respectively, for equipment and 2.5% for depreciable road properties. However, for rail, ties and other track materials, instead of depreciation accounting, the companies follow an acceptable alternate practice of "replacement" accounting. Under this method, replacements in kind are charged to expense while additions and betterments (improvements) are capitalized. The amounts capitalized are not depreciated and are charged against income only when the related properties are retired. Normal retirements of depreciable property are charged to the appropriate depreciation reserve at cost less salvage. At December 31, 1976 and 1975, consolidated nondepreciable properties, including land and land rights, were approximately $568,000,000 (net of approximately $49,236,000 of allocated credit excess discussed in Note 2) and $601,000,000 (restated), respectively.

REPORT OF INDEPENDENT ACCOUNTANTS

Price Waterhouse & Co.

To the Stockholders and Board of Directors of
MISSOURI PACIFIC RAILROAD COMPANY

In our opinion, the accompanying consolidated balance sheets and the related statements of consolidated income, retained income, and changes in financial position present fairly the financial position of the Missouri Pacific Railroad Company and its subsidiaries at December 31, 1976 and 1975, and the results of their operations and the changes in their financial position for the years then ended, in conformity with generally accepted accounting principles consistently applied. Our examinations of these statements were made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

Price Waterhouse & Co.

St. Louis, Missouri
February 14, 1977

Excess of net assets (at acquisition) of consolidated subsidiaries over carrying value of investments was not amortized during 1976 and 1975 (see Note 2).

Federal income taxes — The accompanying consolidated financial statements include provisions for current and deferred federal income taxes. Current federal income taxes have been reduced by the benefits of tax deductions for accelerated depreciation and amortization of properties in advance of such deductions for financial statement purposes. These benefits have been partially offset by the effects of financial statement expense accruals for casualties and other matters which are not deducted for income tax purposes until paid. The net current benefit of these timing differences has been offset by a provision for deferred federal income taxes.

Investment tax credit is accounted for under the flow-through method as realized in the tax return.

Per share data — Earnings per common and common equivalent share include the Preferred Stock as a common stock equivalent on a one-for-one basis. The weighted average numbers of common shares and common share equivalents outstanding during 1976 and 1975 were 12,731,476 and 12,506,990, respectively.

Pensions — The companies have a funded, noncontributory pension plan for substantially all "nonscheduled" (nonunion) employees. Related charges to operating expense represent accruals which include normal cost and amortization of prior service cost over a 35-year period ending January 1, 2001, plus interest on the recorded unfunded pension liability. Pension charges are funded over a 30-year period ending January 1, 2006. As of January 1, 1976, the companies have amended their pension plan as described in Note 5.

Casualty losses — Casualty losses not covered by insurance are accrued and charged to income as they are incurred (see Note 7).

Debt and related expenses — Discount and expense applicable to long term debt is deferred and amortized over the lives of the respective issues using the bonds outstanding method. Gain on reacquisition of bonds is recorded as income.

NOTE 2 — MERGER:

The merger of The Texas and Pacific Railway Company (T&P) and the Chicago & Eastern Illinois Railroad Company (C&EI) into the Missouri Pacific Railroad Company was consummated as a statutory merger as of October 15, 1976 (see Page 3 for additional details). The T&P and C&EI were 96.7% and 78.3% owned, respectively, by the Company at December 31, 1975. Assuming that the merger had occurred and the 972,772 shares had been issued as of January 1, 1975, net income would have been increased by the income applicable to minority interest of $2,967,000 and $2,615,000 and earnings per common and common equivalent share would have been decreased $.08 for each of the years ended December 31, 1976 and 1975.

The merger was accounted for under the "purchase" method of accounting. Under this method, $65,371,000 of excess of net assets (at acquisition) of consolidated subsidiaries over carrying value of investments (including $11,552,000 of "excess" generated at the date of exchange) was allocated to the railroad properties acquired based upon their relative fair values. As a result of this allocation, net road and equipment properties presented in the accompanying consolidated balance sheet for 1976 have been reduced $59,426,000 and $5,945,000, respectively.

NOTE 3—FEDERAL INCOME TAXES:

As described in Note 1, provisions for deferred federal income taxes result from timing differences in the recognition of revenue and expense for tax and for financial statement purposes. The sources of these differences and the tax effect of each are as follows:

	Year Ended December 31,	
Source	1976	1975
	(In Thousands of Dollars)	
Excess of tax over book depreciation and amortization	$15,892	$13,596
Financial statement expense accruals for casualties and other matters which are not deducted for tax purposes until paid	(6,553)	(4,042)
Reduction of property base for gain on reacquisition of bonds	3,228	257
IRS adjustments of 1971 and 1972 tax years—		
Maintenance of way expenses capitalized		(1,018)
Improvements and repairs capitalized		(1,326)
Other	(384)	(1,975)
Provision for deferred federal income taxes	$12,183	$ 5,492

Total tax expense amounted to $30,046,000 for 1976 and $19,832,000 for 1975, an effective tax rate of 29.5% and 28.7%, respectively. The differences between the effective rates and the federal income tax rate of 48% result primarily from investment tax credit, which has been applied under the flow-through method, as shown below:

	Year Ended December 31,			
	1976		1975	
	Amount	% of pre-tax income	Amount	% of pre-tax income
	(In Thousands of Dollars)			
Tax expense computed at federal income tax rate	$48,820	48.0	$33,198	48.0
Reduction in taxes resulting from investment tax credit	(17,793)	(17.5)	(13,351)	(19.3)
Other	(981)	(1.0)	(15)	
Actual tax expense	$30,046	29.5	$19,832	28.7

The Tax Reform Act of 1976 contains a provision which will permit railroads to utilize available investment tax credits to offset up to 100% of their federal income tax liability in 1977 and 1978. Beginning in 1979, the investment tax credit limitation will be reduced 10% annually until it returns to a 50% limitation in 1983. At December 31, 1976, investment tax credit carryovers of approximately $23,000,000 are available to the Company for utilization in such manner. Of the $23,000,000 carryover, $1,700,000 will expire in 1981, $5,700,000 in 1982 and $15,600,000 in 1983, if not used.

NOTE 4— STOCKHOLDERS' EQUITY:

During 1976, the Missouri Pacific Corporation increased its ownership in the Company from 66.3% to 92.3% as a result of an exchange offer completed on June 25, 1976 and a conversion of its Missouri Pacific Preferred into Common Stock on July 16, 1976.

In October, 1976, 972,772 shares of the Company's Common Stock were issued in connection with the merger described in Note 2.

On December 2, 1976 the Company called for the redemption, effective January 17, 1977, of all of its outstanding Preferred Stock at a price of $20 per share plus accrued dividends of $.045 per share. Prior to January 17, 1977, each share of Preferred Stock was convertible, subject to certain dilution provisions, into one share of Common Stock. At December 31, 1976, 156,560 shares of Common Stock were reserved for such conversion. During 1976 and 1975, 5,561,343 and 2,036,924 shares, respectively, of Preferred Stock were converted into Common Stock. The Common Stock account was credited with the stated value of the converted Preferred shares which increased, on a per share basis, the stated value of all shares of outstanding Common Stock. The Common Stock has a stated value of $15.09 and $11.22 per share at December 31, 1976 and 1975, respectively.

The provisions of the mortgages and indenture relative to priority of call in each year upon "Available Net Income" (as defined therein) have been satisfied and no restriction under the mortgages and indenture exists on the Company's retained income at December 31, 1976.

NOTE 5— RETIREMENT PLAN:

The companies amended their pension plan, effective January 1, 1976. The amendments extend pension plan eligibility to substantially all "nonscheduled" (non-union) employees of the companies and conform the plan to the requirements of the Employee Retirement Income Security Act of 1974 which include minimum funding and vesting provisions. Pension expense calculated as described in Note 1 resulted in charges to operating expense in 1976 and 1975 of $7,167,000 and $4,323,000, respectively. Pension expense increased in 1976 as a result of plan amendments and changes in actuarial assumptions as to interest earnings, salaries and railroad retirement benefits. The actuarially computed value of vested benefits and benefits pertaining to retired employees exceeds the market value of the pension fund and the recorded pension liability by approximately $25,900,000 at December 31, 1976.

NOTE 6 — LEASED ASSETS AND LEASE COMMITMENTS:

The Company and its railroad subsidiaries lease a general office building, computer equipment and transportation equipment under long term and contingent lease agreements. Substantially all of the Company's long term transportation equipment leases meet the criteria of a capital lease as defined by Statement of Financial Accounting Standards No. 13 (SFAS 13) "Accounting for Leases" which was issued in November, 1976 by the Financial Accounting Standards Board. SFAS 13 defines a capital lease generally as one which transfers benefits and risks of ownership to the lessee, and requires that, for such leases entered into on or after January 1, 1977, the present value of minimum lease payments be recorded as an asset and an obligation. However, capitalization of such leases existing at December 31, 1976 is not mandatory until 1981, at which time retroactive application is required.

A summary of rental expense charged to operations is presented below. For comparative purposes, amounts for 1975 have been reclassified to reflect the accounting treatment prescribed by SFAS 13. Such amounts were previously reported in accordance with criteria prescribed by the Securities and Exchange Commission.

	Year Ended December 31,	
	1976	1975
Minimum rentals under long term capital leases	$ 8,465,000	$ 7,724,000
Minimum rentals under long term operating leases	2,421,000	2,868,000
Contingent rentals under operating leases (net) —		
Hire of transportation equipment	46,208,000	37,067,000
Joint facility	6,253,000	5,279,000
Computer equipment	2,200,000	2,718,000
	57,082,000	47,932,000
	$65,547,000	$55,656,000

As of December 31, 1976, minimum rental commitments under long term leases were as follows:

Year or Period	Capital leases	Operating leases
1977	$ 9,478,000	$ 2,425,000
1978	9,521,000	2,479,000
1979	10,005,000	2,478,000
1980	9,903,000	2,270,000
1981	9,802,000	1,680,000
1982 through 1992	59,845,000	6,683,000
Total	$108,554,000	$18,015,000

At December 31, 1976, total minimum rental commitments pertaining to capital leases was comprised of the present value of such commitments ($68,058,000) and of interest calculated at the Company's "incremental borrowing rate" at the inception of the leases ($40,496,000). On the assumption that SFAS 13 had been applied retroactively to January 1, 1975, leased assets and obligations at December 31, 1976 and 1975 would have been recorded as follows:

	1976	1975
Leased equipment under capital leases, net of accumulated amortization of $18,830,000 and $13,667,000, respectively	$61,280,000	$58,320,000
Obligations under capital leases —		
Current	$ 3,779,000	$ 2,920,000
Long term	64,279,000	59,935,000
	$68,058,000	$62,855,000

On the assumption that the leases had been capitalized as shown above, and the assets amortized on a straight-line basis over the life of the leases and interest expense computed on the basis of the present value of the declining outstanding balance of the lease commitments, the impact on net income for the years ended December 31, 1976 and 1975 would not have been material.

The Company's leases on transportation equipment provide options to purchase the equipment at fair market value at the expiration of the leases. The lease on the general office building provides an option to renew the lease for four terms of five years each beginning in 1991 and an option to purchase the building for $6,000,000 at any time during the remaining life of the lease.

NOTE 7 — CONTINGENT LIABILITIES:

The Company is contingently liable as guarantor, together with other owner railroads, for principal and interest of certain obligations of various affiliated companies aggregating approximately $129,169,000 at December 31, 1976. Under terms of a service interruption policy, the Company and its railroad subsidiaries are contingently liable for additional premiums up to a maximum of $22,331,000 in the event of work stoppages on other participating roads.

The companies have an insurance deductible of $5,000,000 per occurrence with respect to casualty losses resulting from destroyed equipment, freight loss and damage, personal injury, third party liability and fire and extended coverage risks. At December 31, 1976, the Company has set aside $5,600,000 in capital, insurance and other funds to be used in the event of major uninsured losses.

NOTE 8 — QUARTERLY FINANCIAL DATA (UNAUDITED):

Selected quarterly financial data for 1976 and 1975 appears on page 10.

Condensed Statement of Consolidated Income For The Five Years Ended December 31, 1976

(In Thousands of Dollars Except Per Share Data)

	1976	1975	1974	1973	1972
Operating Revenues	$1,013,668	$888,546	$889,857	$753,582	$642,919
Operating Expenses	747,242	667,694	673,315	584,296	508,284
Net Revenue from Operations	266,426	220,852	216,542	169,286	134,635
Other Operating Charges	141,161	117,238	118,573	97,439	70,737
Other Income (Net)	22,217	9,649	16,373	16,070	5,679
Interest Expense	45,773	44,101	41,648	38,600	37,107
Income Before Federal Income Taxes and Minority Interests	101,709	69,162	72,694	49,317	32,470
Provision for Federal Income Taxes:					
Current	17,863	14,340	13,609	6,433	2,681
Deferred	12,183	5,492	7,058	10,043	11,426
Less — Income Applicable to Minority Interests	2,967	2,615	2,305	1,946	1,733
Net Income	$ 68,696	$ 46,715	$ 49,722	$ 30,895	$ 16,630
Per Share Data:					
Earnings Per Common and Common Equivalent Share	$ 5.40	$ 3.74	$ 3.98		
Cash Dividends Paid:					
Preferred	1.00	1.00	1.00		
Common	1.25	1.20	1.10		
Class A				$ 5.00	$ 5.00
Class B				20.00	5.00

Because of the characteristics of Missouri Pacific's Class A and Class B stock outstanding prior to the January, 1974 recapitalization, earnings per share data based thereon have been omitted for the years 1972 and 1973. Per share dividends and earnings for 1974 reflect the five-for-one stock split of July 5, 1974.

Management Discussion and Analysis of Statement of Income

Year 1976 vs 1975

With a general improvement in business conditions, operating revenues in 1976 climbed 14.1% to an all-time high. An increase of 6.8% in revenue ton miles, rate increases yielding more than 7% over 1975 and a favorable change in traffic mix were all factors contributing to the record revenues.

Operating expenses for 1976 increased by 11.9%. Material and supply costs continued their rising trend during 1976, increasing more than 6%. Wage and labor costs also rose due mainly to a 3% general wage increase, effective April 1, and cost-of-living increases granted in January and July.

Other operating charges were up substantially in 1976, increasing by $23.9 million over the previous year. Unemployment taxes rose $1.5 million, or almost 35%, due to an increase in the tax rate from 4.0% to 5.5% while Railroad Retirement taxes climbed more than $10.2 million mainly as a result of an increase in the maximum taxable base. In addition, net amounts paid other railroads and private car lines for use of their equipment rose by $8.7 million in 1976.

Other income (net) in 1976 more than doubled that of the previous year, increasing $12.6 million. Increases of $6.2 million from profit on Company bonds reacquired, $2.4 million of income from less than majority-owned subsidiaries and $1.5 million in interest income were the main reasons for the substantial rise.

Interest expense for 1976 increased almost $1.7 million due to equipment obligations issued to finance the large amount of new car purchases made during the year.

An explanation of the fluctuation in federal income taxes for 1976 vs 1975 is included in Note 3 of Notes to Consolidated Financial

Statements. The basis for computing the tax and the reasons for any fluctuations in other years are not significantly different.

Year 1975 vs 1974

In a year of generally depressed business conditions, operating revenues were only slightly lower than the previous year. A 12.7% decline in revenue ton miles was substantially offset by freight rate increases yielding about 13% after exceptions.

Controlled expense reductions to offset the downturn of business in general resulted in a reduction in the average number of employees of 9.9%. Higher prices for material and supplies coupled with wage increases of 10%, effective January 1, and 5%, effective October 1, were the main factors causing increases in operating expenses. The net result was a decrease of less than 1%.

Other income (net) was down $6.7 million in 1975 as compared to the previous year. This decline was mainly due to decreases in interest income of $2.7 million, income from less than majority-owned subsidiaries of $1.9 million, and $0.5 million from gain on Company bonds reacquired and from an increase of $0.4 million from the write-off of receivables from bankrupt railroads.

Computation and Application of Available Net Income

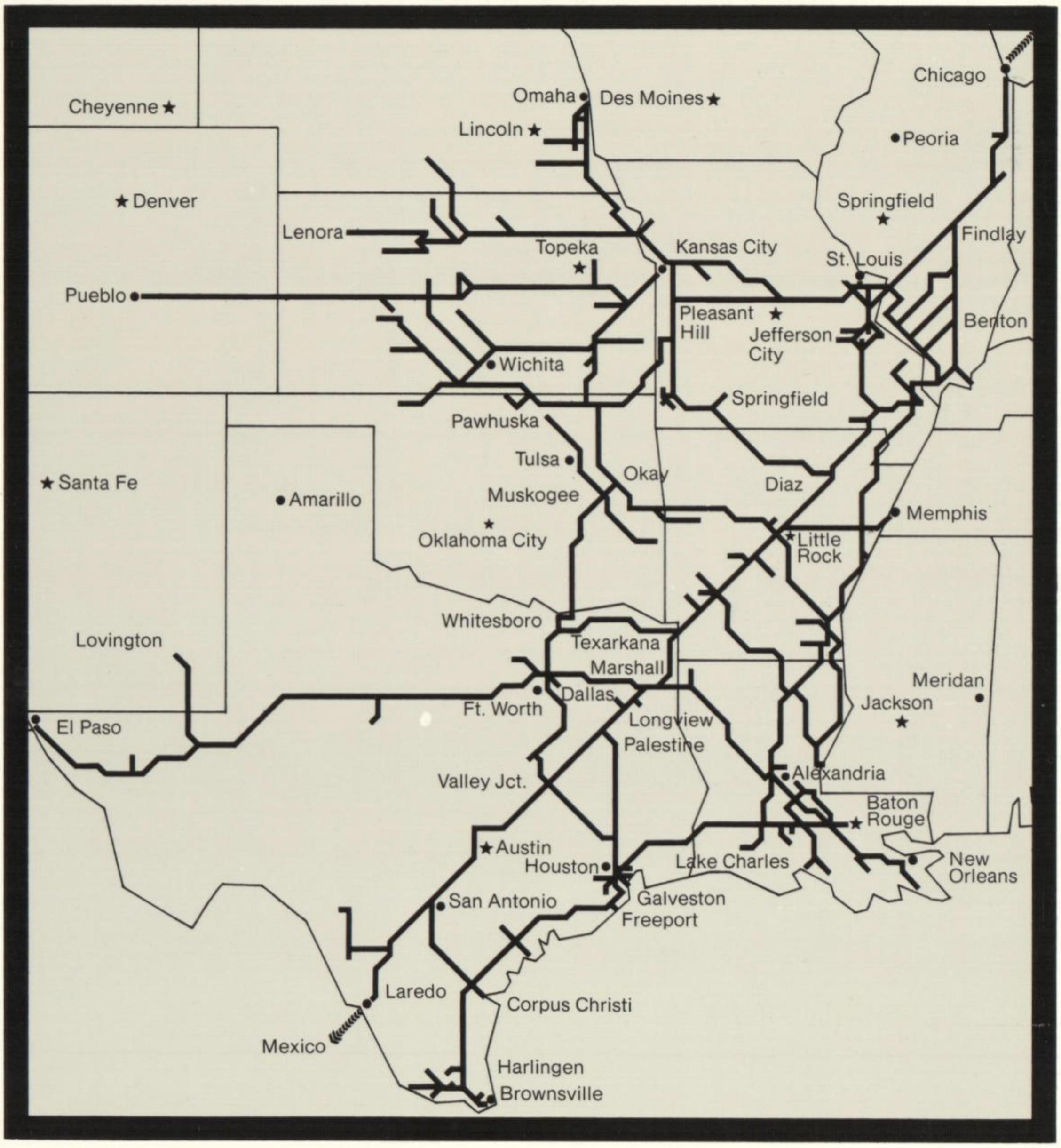
Income of Missouri Pacific Railroad Company and its Wholly-Owned Railway Companies (as required by the Company's Mortgages and Indenture) (In Thousands of Dollars)

	1976	1975
Income Before Fixed Charges and After Federal Income Taxes	$ 91,716	$66,624
Income of Wholly-Owned Railway Companies Before Fixed Charges	30,957	3,559
Road Property Retired and Credited to Operating Expenses	(29)	(138)
	122,644	70,045
Less — Dividends of 100% Railway Companies Included in Missouri Pacific Income	5,558	3,682
Total Income Available for Fixed Charges	117,086	66,363
Fixed Charges	35,303	24,260
Available Net Income	81,783	42,103
Capital Expenditures Fund	15,737	10,027
Remaining Income	66,046	32,076
Sinking Fund on First Mortgage Bonds	771	771
Remaining Income	65,275	31,305
Interest on General Mortgage Bonds, Series A	2,451	2,542
Remaining Income	62,824	28,763
Sinking Fund on General Mortgage Bonds, Series A	350	350
Remaining Income	62,474	28,413
Interest on General Mortgage Bonds, Series B	2,330	2,358
Remaining Income	60,144	26,055
Sinking Fund on General Mortgage Bonds, Series B	338	338
Remaining Income	59,806	25,717
Interest on Income Debentures	5,001	5,001
Remaining Income	54,805	20,716
Sinking Fund on General and Refunding Mortgage Bonds, (T&P)	1,456	
Remaining Income	53,349	20,716
Sinking Fund on First Mortgage Bonds (KO&G)	66	
Remaining Income	53,283	20,716
Sinking Fund on Income Debentures (C&EI)	123	
Balance	$ 53,160	$20,716

MISSOURI
PACIFIC
SYSTEM

MISSOURI PACIFIC SYSTEM

The Mo-Pac System totals nearly 12,000 miles of railroad supplemented by 18,000 miles of highway routes. It has railroad operations in 12 states in the midwest, south and southwest, and through its subsidiaries also performs a wide variety of intermodal services including trucking, piggyback, containerization, less-than-truckload freight and airfreight forwarding.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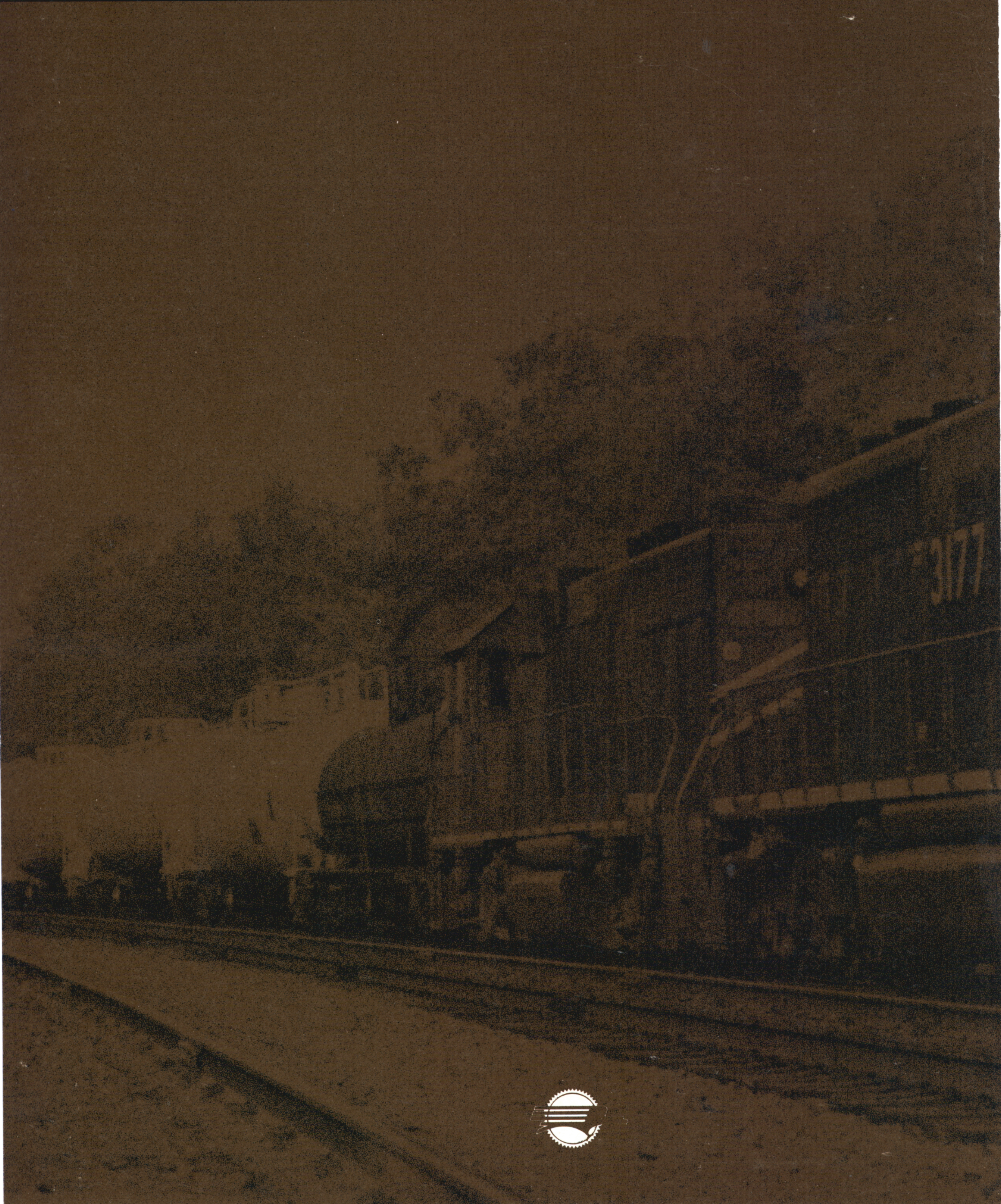
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